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INFO RUEHZL/EUROPEAN POLITICAL COLLECTIVE PRIORITY  
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RUCPDO/DEPT OF COMMERCE WASHDC PRIORITY

C O N F I D E N T I A L SECTION 01 OF 02 BRUSSELS 001702

SIPDIS

E.O. 12958: DECL: 11/06/2023

TAGS: [ECON](#) [EFIN](#) [BE](#)

SUBJECT: AMBASSADOR'S MEETING WITH BELGIAN FINANCE MINISTER  
ON THE FINANCIAL CRISIS AND ITS IMPACT

Classified By: POL/ECON Counselor Richard Eason, Reasons 1.4 (b) and (d).

¶1. (C) SUMMARY: Belgium's Finance Minister Didier Reynders expects the EU's number one goal in the November 15 Finance Summit to be to build collaborations between governments and with the IMF over the coming weeks. The rescue of Fortis by Belgium, the Netherlands and Luxembourg is an example of what can be done with cross-European collaboration. Reynders believes that the next challenge for governments will be to rescue distressed companies with financial problems. He expects 12-18 months of more economic instability and traces the current crisis to the failure of Lehman Brothers. Rising unemployment and the fall-out of the financial crisis will become a key political issue in the run-up to the June 2009 regional elections, generating a debate on the merits of liberalism versus socialism, particularly in Wallonia. Regarding the financial crisis in Belgium, there are still problems related to inter-bank financing and a resulting depressed level of new business activity. Belgium continues to be eager to see whether Dexia's U.S. monoline subsidiary, FSA, will be covered by the Paulson Plan. END SUMMARY.

#### THE FINANCIAL CRISIS

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¶2. (C) Finance Minister and Deputy Prime Minister Didier Reynders met with the Ambassador on November 4 to discuss the financial crisis and its impact on Belgium. Reynders noted that he was in regular contact with officials of the U.S. Treasury and the Federal Reserve Bank. These discussions centered on the Paulson Plan and the crises affecting banks and insurance companies in Europe. Belgium continues to have significant exposure in Dexia through its U.S. monoline subsidiary FSA. Belgium is working with the French, the Fed and the U.S. Treasury to reach a solution but is being told that the solution has to lie with the Treasury Department. Reynders said he may seek the Embassy's good offices on the issue at some point in order to find a solution with the U.S. government.

¶3. (C) Reynders had just returned from a European Union ECOFIN meeting and was meeting with the head of Belgium's Banking Commission and a Director of Belgium's central bank as the Ambassador arrived. Reynders said the ECOFIN meeting was held to prepare for the November 15 G-20 meeting in the U.S. The EU will want to discuss concrete cases like Dexia. It will also want to discuss global collaboration on dealing with the crisis and attempt to develop a central vision of the future of the world's financial architecture with concrete proposals. On Friday, November 7, French President Sarkozy will chair a summit in Brussels to finalize the EU position for the G-20 meeting. The first goal of the EU will be to lay out a plan of collaboration between governments for the coming weeks which will also lay out the role of the IMF.

¶4. (C) Reynders sees the resolution of the Fortis crisis as

an example of how an EU-wide collaboration would work in responding to a bank failure, based on the fact that the governments of the Netherlands, Belgium and Luxembourg had coordinated on the solution. Reynders did not expect the EU to establish a pool of capital for use in crises. He noted that the support program for Hungary involved both the EU and the IMF.

15. (C) According to Reynders, EU governments had injected 280 billion euros into banks across Europe in exchange for shares and had established an additional 1.8 trillion euros in government guarantees for refinancing. Dexia had drawn on 150 billion of these guarantees. The guarantees were valid for periods ranging from three months to three years.

16. (C) Based on the European Commission's forecast of 0.1 percent growth for the eurozone, Reynders expects governments will have to bail out companies as well, as the financial crisis and credit crunch hits the real economy. This is already happening in Belgium, despite improvements in the liquidity picture.

17. (C) Reynders expects another 12-18 months before Europe begins to work itself out of the crisis. He asserted that the trigger for the crisis was clearly the failure of Lehman Brothers. Letting Lehman Brothers fail, although he understood for rationale for it, was "a mistake." It caused a contagion of a lack of confidence which swept through the financial system.

#### THE POLITICAL IMPACT

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18. (C) In looking forward to Belgium's regional elections in June 2009, Reynders expects a vigorous debate in the country on the merits of liberalism versus socialism. (NOTE: Reynders heads the francophone liberal party and is in a difficult campaign with the long-entrenched francophone socialists for political influence, particularly in Wallonia. END NOTE.) The expected low growth will inevitably fuel higher unemployment. Although Belgium averages 7% unemployment nationally, unemployment is far higher in Wallonia and Brussels. Indeed, in the under 25 age cohort, it can be 25% to 30%. Already the steel company Arcelor Mittal is shutting a steel mill in Wallonia. Other companies doing the same will only lead to more job losses, particularly in Wallonia.

19. (C) The financial crisis has temporarily shelved the political debates on institutional reform. However, Belgium must still have a national discussion on autonomy for the regions as a possible means of solve the unemployment problems. The north of Belgium (Flanders) continues to have problems finding jobs for older workers and the south problems finding jobs for younger workers.

#### THE ECONOMIC IMPACT

110. (C) Thanks in part to support from the European Central Bank as well as from the Belgian government, the liquidity situation in Belgium is improving. However, there are still problems with the cost and availability of financing between banks. But the real problem is that little new business activity is being generated. Liquidity is available in the markets but is not being used. Money is injected into the markets in the morning but twice the arm is turned in each night. Many companies continue to be afraid to invest. Banks are holding on to their cash and do not want to make any investments with it. Just last week, the government in Belgium agreed to provide funding to small and medium enterprises, an attempt to compensate for the sharp drop in demand for loans by SMEs.

¶11. (C) Regarding government debt, Reynders noted that Belgium's debt/GDP ratio had reached 140% in 1993. It was around 80% today. This helps give the government some flexibility and the ratio could rise to 87% of GDP as a result of the bank bail-outs.

#### DEXIA AND FSA

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¶12. (C) The Belgians are working closely with the French and the U.S. Treasury and the Fed on the package for Dexia. A key challenge is the bank's exposure to its U.S. monoline subsidiary, FSA. The Belgians are eager to learn whether FSA will be covered by the Paulson plan.

#### COMMENT

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¶13. (C) Reynders and staff at the Finance Ministry and Central Bank are exhausted from their weeks of crafting bail-outs or packages for Belgium's three main banks and in trying to jump-start the credit markets. Analysts give the government generally good marks, despite the radical transformation suffered by the country's banking sector. The issue for Reynders will be whether francophone voters will blame him for the crisis, based on the fact that he has been Finance Minister for nine years. The francophone socialists will certainly try to use the crisis against him politically.

In a sense, the June regional elections will be a test on how much views of an open economy with less involvement by the state has become accepted by average Belgians, especially those living in Wallonia, which has been ruled for decades by the Socialist Party.

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